

UNDERSTANDING THE RESPONSIBILITIES OF PUBLIC FUND INVESTING

California Debt and Investment
Advisory Committee

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Presenters:

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Overview – San Francisco

- Total Portfolio - \$3.54 billion
- Serves as Treasurer for City & County of San Francisco, San Francisco Unified School District, and San Francisco City College. County entities include: Airport, Public Utilities Commission, Hospital System, Transit System, Port, and Development Authority.

Overview – San Francisco- cont.

- Department Staff (11)
 - Chief Assistant Treasurer
 - Investment Officer
 - Investment Analyst
 - Treasury Operations Manager
 - Cash Manager
 - Principal Accountant
 - Accounting Clerks (5)

Overview – San Francisco- cont.

- Portfolio (6/30/07)
 - Average weighted maturity – 126 days
 - Portfolio fully managed in-house

Overview – Contra Costa County

- Total Portfolio- \$2.34 billion
- Serves as Treasurer for Contra Costa County, 18 school districts, Board of Education, Contra Costa Community College District and 21 other public agencies
- Department Staff (7)
 - Assistant Treasurer
 - Investment Officer
 - Investment Operations Analyst
 - Treasurer's Accounting Officer
 - Accountant III
 - Accounting Tech –2

Overview – Contra Costa County- cont.

- Portfolio (6-30-07)
 - Yield to maturity investor
 - Average weighted maturity- 86.53 days
 - 72.7% managed in-house
 - 24.4% Outside Contractors (LAIF, GIC's, Wells Fargo Asset Management, Columbia Management Group – BofA, CalTRUST)
 - 2.9% cash

A Very Different Model - Emeryville

- Previously served as Finance Director and Treasurer for the City of Emeryville
- Total Portfolio - \$210 million
- Treasury & Investment Staff (2)
 - Finance Director
 - Accountant

Definition (Gov't Code 53600)

- As used in this article, “local agency” means county, city, city and county, including a chartered city or county, school district, community college district, public district, county board of education, county superintendent of schools, or any public or municipal corporation.

Responsibility for Investments

- **Governing Body** (Gov't Code Sections 27000.3 and 53600.3) **is responsible**, but may designate authority for a one-year period to a fiduciary.
- Once delegated, a county board of supervisors may not set conditions with respect to contracts for investment management services executed by the treasurer (Attorney General Opinion #04-1203, May 11, 2005)

Responsibility for Investments (Gov't Code 53607)

- “The authority of the legislative body to invest or to reinvest funds of a local agency, or to sell or exchange securities so purchased, may be delegated for a one-year period by the legislative body to the treasurer of the local agency, who shall thereafter assume full responsibility for those transactions until the delegation of authority is revoked or expires, and shall make a monthly report of those transactions to the legislative body. Subject to review, the legislative body may renew the delegation of authority pursuant to this section each year.”

Standards for Governing Bodies or Persons Authorized to Make Investment Decisions for Local Entities (Gov't Code 53600.3)

- "...all governing bodies of local agencies or persons authorized to make investment decisions on behalf of those local agencies investing public funds pursuant to this chapter are trustees and therefore fiduciaries subject to the prudent investor standard."

Investment Standards

- All fiduciaries must follow the **Prudent Investor Standard** in that *"a trustee shall act with care, skill, prudence, and diligence under the circumstances then prevailing, including, but not limited to, the general economic conditions and the anticipated needs of the agency, that a prudent person acting in a like capacity and familiarity with those matters would use in the conduct of funds of a like character and with like aims..."*

Trustee Objectives Regarding Funds

(Gov't Code Section 53600.5)

- When investing, reinvesting, purchasing, acquiring, exchanging, selling, or managing public funds, the primary objective of a trustee shall be to **SAFEGUARD THE PRINCIPAL** of the funds under its control.
- The second objective shall be to **MEET THE LIQUIDITY** needs of the depositor.
- The third objective shall be to **ACHIEVE A RETURN** on the funds under its control.

Key Provisions of Investments

- **Safety**...Preservation of Principal
- **Liquidity**...Able to meet cash flow needs without requiring the sale of securities
- **Yield**...last consideration, but often the only measurement of investment success

Safe and Liquid Investments

- Safety and Liquidity are linked
 - Lack of liquidity could lead to early sale of investments and loss of principal
- Legal does not necessarily mean safe
 - Remember the “Prudent Investor Standard”

Yield

- Avoid chasing yield
- Disciplined approach
- Benchmark to an appropriate standard to justify disciplined approach
 - Avoid comparing to other jurisdictions
 - Consider index with similar mix of securities and fund duration

Additional Investment Criteria

- San Francisco:
 - In addition to Safety, Liquidity and Yield, San Francisco has added a social responsibility criterion in a subordinate role.
 - Look at Social Responsibility when choice is substantially equivalent on Safety, Liquidity and Yield
 - Encourage investments that:
 - Support community well-being through safe and environmentally sound practices and fair labor practices.

Additional Investment Criterion- cont.

- Support equality of rights
- Offer banking products to serve all members of the local community
- Promote community economic development
- Discourage investments in entities that:
 - Manufacture tobacco products, firearms, nuclear weapons
 - Finance high-cost check-cashing and payday-lending

Additional Investment Criterion- cont.

- Contra Costa County:
 - All legal securities issued by a tobacco related company are prohibited. A tobacco related company is defined as an entity that has revenues of 15% or more from the sale of tobacco related products.

Investment Limitations

- Limitations:
 - Government Code 53600 *et seq*
 - Adopted Investment Policy
 - Must conform to State Law
 - May be more restrictive
 - Prudent Investor Standards

Investment Approach

- Perform cash flow analysis
 - One month/six months/one year/etc.
- Determine short-term vs. long-term investment portfolio
- Develop range of investment options for each portfolio type
- Determine ability to pool funds from different sources

Developing an Investment Policy

- Government Code Requirements
- Purpose of an Investment Policy
- Components of a Policy
- Oversight- The Critical Element

Government Code Requirements

- Prior to AB 2853 (GC 27131 (a) and (b)), the Treasurer was to submit a quarterly report to the governing board within 30 days following the end of the quarter covered by the report containing the following:
 - Type of investment, issuer, date of maturity, par value, and dollar amount invested

Government Code Requirements- cont.

- Description of any investments under management of contracted parties, including securities lending programs
- Description of the compliance with the statement of investment policy
- Statement denoting local agency's ability to meet expenditure requirements for the next six months

Government Code Requirements- cont.

- For funds under management of outside party that is not a local agency or LAIF, report must include current market value and source or validation
 - Subsidiary ledger of investment may be used in accordance with GAAP
- Additional information as required by agency's governing body

Government Code Requirements- cont.

- Funds deposited in LAIF, county pools, FDIC or NCUA insured accounts, or combination of these, may use most recent statements in lieu of above requirements

Purpose of an Investment Policy

- To establish procedures and guidelines that will ensure the prudent management of public agency funds
- To incorporate all of the regulations specified by California Code sections into the agency's investment program
- To specify the risk tolerance and investment philosophy of the agency

Components of a Policy

- Policy Statement
- Scope
- Investment Objectives
- Prudence
- Delegation of Authority
- Safekeeping and Custody of Securities
- Diversification
- Maximum Maturities
- Ethics and Conflicts of Interest

Components of a Policy- cont.

- Authorized Financial Institutions
- Authorized Investments
- Collateralization
- Internal Control
- Performance Standards
- Reporting Requirements
- Policy Adoption
- Glossary of Terms

Oversight- The Critical Element of Success

- Create the Internal Controls- for smaller entities controls are probably developed by consultation between agency and outside auditors. May not be part of “oversight” as described here.
- Establish Review Process
- Monitor Investment Reports for Conformance to Policy Guidelines

Oversight- The Critical Element of Success- cont.

- **Treasury Oversight Committees** (GC 27131 & 27132.1-27132.4) –This is for Counties. Other agencies may have a different structure.
 - Consist of 3 – 11 members
 - Monitor and review the county investment policy. If a TOC is established, then an Investment Policy is required. (GC 27133)

Oversight- The Critical Element of Success-cont.

- Conducting or causing an annual audit and discussing their findings at a public meeting
- Gives local agencies and private sector a say in the policies governing the investment pool
- Oversight committees can not interfere in the day-to-day operations of the Treasury
- **The bottom line... OVERSIGHT IS GOOD**

An Investment Policy is not required by statute ...but

- An investment policy should always be in place. While no longer required by statute, it is in the best interest of the local agency to present and discuss the policy with the agency's legislative body and/or oversight committee and then have the policy approved by a vote of the legislative body. A public vote signifies that the legislative body shares a fiduciary responsibility with the Treasurer, increases the authority and legitimacy of the investment policy, and provides transparency and disclosure.¹

— ¹Local Agency Investment Guidelines 2007, page 4, CDIAC

Contra Costa County Treasury Oversight Committee

- Composed of 7 members:
 - One representative appointed by the Bd of Sups
 - The County Superintendent of Schools or designee
 - One representative selected by the school districts and community college district
 - One representative selected by the special districts
 - Three members of the public nominated by the County Treasurer who shall have expertise in, or an academic background in public finance and investment

Contra Costa County Treasury Oversight Committee- cont.

- Meets quarterly
- Causes an annual audit of the Treasury to be conducted
- Reviews and approves the Investment Policy, and all Investment Reports. Forwards to the Board of Supervisors for their acceptance.

San Francisco Treasury Oversight Committee

- Composed of 5 members
 - Controller
 - School District Representative
 - Community College District Representative
 - Major CCSF Pool Participant
 - Member of the Public
- Oversight committee has similar role to Contra Costa County

San Francisco Treasury Oversight Committee- cont.

- Meets quarterly (most of the time)
- Causes annual audit of the Treasury to be conducted
- Reviews investment performance
- Reviews investment policy annually
- SF TOC has lower level of involvement than Contra Costa County

Emeryville Treasury Oversight

- Irregular meetings of the Finance Committee of the City Council
- Monthly reporting to City Council

Best Practice

- Each non-county local agency should consider for itself if an oversight committee is appropriate based on its current oversight procedures, complexity of its portfolio, frequency with which it purchases securities, and skill level of its staff. The limitations and restrictions associated with county treasury oversight committee members do not apply to committees formed by other local government entities.¹

— ¹ Local Investment Agency Guidelines 2007, Page 35, CDIAC

Issuing Periodic Investment Reports

- Purpose of the Reports
 - Convey required investment portfolio facts at a specific point in time
 - Agencies with smaller and simpler portfolios will have simpler reports
 - Include additional information as determined by the Treasurer, governing board, or oversight committee (optional items)
 - Economic outlooks narrative
 - Comparison of current period to prior period(s)

Issuing Periodic Investment Reports- cont.

- Information that adds depth to the report
- Simple information such as where the yield curve is going
- Economic/public finance reports written by industry experts
- Comparison of performance to a benchmark (Treasury Index, Lehman Government Bond Index, LAIF, or Combination)
- Opportunity to discuss “Big Picture” items

Critical Issues

- Fund Management
- Risk Management
- Ethics
- Politics

Fund Management

- Paid staff vs. Investment Advisor
- Cash Flow Analysis
- Mix of short-term to longer-term
- Mix of investment types
- Where do you put your liquid funds?
- How liquid do you need your liquid funds to be?

Identify and Manage Risk

- Political Risk
- Credit Risk
 - Securities, dealers, banks
- Liquidity Risk
 - Ability to sell quickly, spread difficulties
- Market Risk
 - Loss of value, mark-to-market, maturity control
- Volatility Risk
- Rate changes Re-Investment Risk
- Event Risk
 - Credit or industry changes
 - Callables

Ethics

- Need for Transparency
- Dealing with Broker/Dealers
 - Level of professional ethics
 - Amount of experience with local agencies
 - Gifts and gratuities
- Making Proper Investments
 - Make investments for the right reasons
 - Follow investment policies

Political Issues

- Pressure to use “friends” for investments
 - Stick to investment policy
 - Have an approved list of broker/dealers
 - Have an investment plan in place
 - Use competition to evaluate any purchase

Form 700- Statement of Economic Interest

- Who must file:
 - Elected and appointed officials in Gov't Code section 87200 (See GC for listing)
 - Employees and appointed officials pursuant to a conflict of interest code. Obtain your disclosure categories, which describe the interests you must report, from your agency.
 - Members of newly created boards and commissions not yet covered under a conflict of interest code.

Form 700- Statement of Economic Interest- cont.

- Must be filed annually. Review very carefully...i.e. gift prohibition, honorarium ban, loan prohibitions, etc.
- An agency can be more inclusive about who files

Form 700- Statement of Economic Interest- cont.

- Gifts- A gift is anything of value for which you have not provided equal or greater consideration to the donor. A gift is reportable if its fair market value is \$50 or more. In addition, multiple gifts totaling \$50 or more received during the reporting period from a single source must be reported. Gifts are reportable regardless of where the donor is located. (see Schedule D, Form 700)
- Gifts are limited by law to a value of \$390 (effective January 1, 2007) in a calendar year from a single source.

- Questions?